No. 82-1766

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,

Respondents.

A. G. BECKER INCORPORATED,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF OF PETITIONER SECURITIES INDUSTRY ASSOCIATION

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QUESTIONS PRESENTED

At issue is an unprecedented administrative construction of the Glass-Steagall Act, the primary federal statute that has governed the structure of the financial services industry in this country since the national banking crisis fifty years ago. The specific questions presented are:

1. Did the majority below err in acceding to a ruling of the Federal Reserve Board that allows banks to underwrite commercial paper, despite the express prohibition in the Glass-Steagall Act against bank underwriting of "notes, or other securities," when even the Board concedes that commercial paper is "notes" within the plain language of the Act and this Court repeatedly has admonished that this statutory language is to be construed broadly and applied literally?

2. Did the majority below err in holding that the Federal Reserve Board is free on a "case-by-case" basis to "adapt" the underwriting prohibition of the Glass-Steagall Act according to its administrative view of the risks involved and regardless of the banks' marketing role, when Congress itself has repeatedly refused to grant any exemptive authority over the Act's flat prohibition to any administrative agency?

PARTIES TO THE PROCEEDING

In addition to the petitioners* and respondents listed in the caption, the following are also respondents in those consolidated actions: Paul A. Volcker as Chairman of the Board of Governors of the Federal Reserve System ("Board"), Frederick H. Schultz, Nancy H. Teeters, J. Charles Partee, Henry C. Wallich, Emmet J. Rice and Lyle E. Gramley as Members of the Board.

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* Pursuant to Rule 28.1 of this Court, petitioner Securities Industry Association states that it is a national trade association representing more than 500 securities brokers, dealers and underwriters who are responsible for over 90 percent of the securities brokerage and investment banking business in the United States.

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PRELIMINARY STATEMENT

This case involves a statutory "interpretation" of the Glass-Steagall Act that sanctions a result Congress itself sought to prohibit through the statute. In order to eliminate the potential for abuses and conflicts of interest inherent in the combination of commercial and investment banking, Congress separated

those activities as completely as possible. Through the Act Congress mandated, not case-by-case regulation of bank underwriting activities, but a flat statutory prohibition.

The Act expressly bars banks from underwriting "notes, or other securities". Refusing to apply this language literally, despite this Court's repeated admonitions to do so, the Board found commercial paper notes are not "notes" or "securities". The Board also applied a functional analysis that ignores the role of banks and permits it administratively to exempt any number of securities from the Act on a case-by-case basis by applying a host of factors found nowhere in the statute.

As will appear, the decision below, upholding the Board's ruling, should be reversed.

OPINIONS BELOW

The opinions of the Court of Appeals for the District of Columbia Circuit (220A)[1] are reported at 693 F.2d 136. The decisions of the Court of Appeals for the District of Columbia Circuit denying a joint petition for rehearing (258A) and suggestion for rehearing *en banc* (260A) are unreported.

The opinion of the District Court for the District of Columbia granting summary judgment in favor of petitioners (194A) is reported at 519 F. Supp. 602. The administrative ruling of the Board (122A) issued in response to petitions by the Securities Industry Association ("SIA") and A. G. Becker Incorporated ("A. G. Becker") is unreported, and the Board's subsequent "Policy Statement Concerning the Sale of Third Party Commercial Paper by State Member Banks" (183A) is reported at 46 Fed. Reg. 29333 (June 1, 1981).

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1 Citations herein to material printed in the Joint Appendix appear as "___A".

JURISDICTION

The judgment of the Court of Appeals for the District of Columbia Circuit was entered on November 2, 1982. A timely petition for rehearing and suggestion for rehearing *en banc* was denied by orders entered on February 2, 1983. A joint petition for certiorari was filed on April 29, 1983; certiorari was granted on October 3, 1983. The Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Two sections of the Glass-Steagall Act are involved here.[2] Section 16 of the Act provides, in relevant part:

> [A national bank] shall not underwrite any issue of securities or stock; . . . .

12 U.S.C. § 24 (Seventh) (Supp. IV 1980).[3] Section 21 of the Act provides, in relevant part:

> [I]t shall be unlawful . . . [f]or any person, firm, corporation, association, business trust, or other similar organization, engaged in the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits subject to check or to repayment upon presentation of a

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2 What is generally known as the Glass-Steagall Act was enacted as part of the Banking Act of 1933, 48 Stat. 162, and is codified in various sections of Title 12 of the United States Code. Relevant to this action are sections 16 and 21 of the Act, 12 U.S.C. §§ 24 (Seventh) and 378.

3 The terms of section 16, which expressly apply to national banks, are also made applicable to state member banks of the Federal Reserve System, such as Bankers Trust Company, by 12 U.S.C. § 335.

> passbook, certificate of deposit, or other evidence of debt, or upon request of the depositor. . . .

12 U.S.C. § 378(a)(1) (1976).

STATEMENT OF THE CASE

A. The Administrative Proceedings

In 1978 Bankers Trust Company ("Bankers Trust"), a state-chartered commercial bank, initiated an aggressive campaign to convince existing and prospective corporate customers to distribute their commercial paper (*i.e.*, unsecured, short-term notes) through the bank, rather than through securities dealers. (*See* 33A; 39A-53A; 59A-69A.) Bankers Trust shortly thereafter began to market third-party commercial paper notes—the first time any bank had done so since the Glass-Steagall Act was adopted by Congress 50 years ago.

The SIA, representing over 90 percent of the securities firms in the country, and A. G. Becker, a major dealer in commercial paper, separately petitioned the Board to declare that the bank's activity violated the Glass-Steagall Act and to order the bank to cease and desist from its third-party commercial paper activity. (196A.)

The Board denied the petitions. (122A, *et seq.*) Although the Board recognized that the issues involved were primarily legal in nature (126A, 143A), conceded that the statute expressly precludes banks from underwriting "notes" (131A), and admitted that commercial paper comprises short-term notes (122A), the Board concluded that the statute should not be accorded a literal reading. (131A.) The Board instead adopted a "functional" analysis which, ignoring the bank's role in distributing the notes, concluded that their sale was the equivalent of a commercial loan to the issuer and therefore that bank participation of any type was appropriate. (135A-136A.)

The Board's ruling also conceded the "potential unsafe and unsound practices" that might proliferate if banks generally

were to begin dealing in commercial paper. (141A.) The Board therefore issued "guidelines" to govern the sale of commercial paper notes by all state bank members of the Federal Reserve System. (182A-189A.) The Board's action thereby not only permitted one bank to engage in these marketing activities, but in effect encouraged all member banks to do likewise.

After the Board's ruling, the SIA and A. G. Becker commenced lawsuits under the Administrative Procedure Act, 5 U.S.C. §§ 701, *et seq.*, before the District Court for the District of Columbia, challenging the ruling as contrary to law.

B. The District Court Decision

On cross-motions for summary judgment, the District Court (Joyce Hens Green, J.) held that commercial paper, which by the Board's own admission constitutes notes, fits squarely within the proscriptions against bank underwriting of corporate "notes" and "securities" set forth in sections 16 and 21 of the Glass-Steagall Act. The District Court refused to accept the narrow statutory construction proposed by the Board, noting that "[t]he statute draws broad lines, leaving no room for administrative amendment." (214A.)

The District Court also rejected the Board's "functional" argument that, because of its relatively short maturity, the nature of its purchasers, and other non-bank related factors, the commercial paper sold by Bankers Trust functions more as a commercial loan than as a security. That analysis was fundamentally incorrect, the District Court concluded, because "it ignores the specific conduct of the bank, glossing over whether the bank purchases commercial paper for its own account, . . . or purchases for future sale to an outside party or arranges a transaction between purchaser and seller." (217A.)

Holding the Board's ruling to be contrary to law, the District Court concluded that the Board had improperly redrawn the congressionally mandated boundary between commercial and investment banking (218A; footnote omitted):

> The realignment of our nation's financial industries is for the elected representatives of our nation to bring to fruition by comprehensive legislation, and not for fiat by judicial decree or by administrative policymaking.

C. The Court of Appeals Decision

In a split decision the Court of Appeals reversed the District Court.

1. The Majority Opinion

The majority's principal reason for reversal was its view that, although the issue presented was purely legal in nature, the Board should be free to "adapt" the statute on a "case-by-case basis" according to the Board's view of "current business reality". (228A.) Despite the broad language of sections 16 and 21 of the Act, prohibiting banks from underwriting all corporate "notes" and "securities," and despite this Court's repeated direction that those terms are *not* to be construed narrowly, the majority concluded that a "narrower meaning" should be accorded the statutory terms. (235A.) In the majority's view, the terms include only "instruments for raising capital as part of the permanent financial structure of a corporation," while "implicitly permitting" banks to underwrite all other types of debt instruments. (236A.)

The majority also addressed the Board's "functional analysis". While recognizing that in certain loan transactions a bank *purchases* commercial paper, the majority held that the bank here "is simply on the other side of the transaction." (246A.) Thus, viewing the role of the bank as immaterial, the majority focused instead on characteristics such as the financial soundness of commercial paper issuers, the sophistication of its purchasers and the relatively low risk nature and short maturity of commercial paper, to conclude that such notes do not give rise to the hazards at which the Glass-Steagall Act was directed. (244A-249A.)

The majority held that the terms "notes" and "securities" in the Act did not encompass "prime quality commercial paper, of maturity less than nine months, sold in denominations of

over $100,000 to financially sophisticated customers rather than to the general public." (249A; footnote omitted.) Significantly, however, it conceded that other commercial paper "of smaller denominations, or issued to the general public," could well be a "note" or "security" under the Act. (250A.) The majority's holding, in short, was premised upon its conclusion that the Board is free to define what "securities" are covered by the Act based solely upon the Board's assessment of the hazards that banks might encounter in underwriting them.

2. The Dissent

Senior Circuit Judge Robb dissented from the majority's analysis, finding that "the majority's holding contravenes the fundamental policy of the Glass-Steagall Act." (250A.) Judge Robb rejected the functional analysis followed by the Board and adopted by the majority, noting, as had the District Court, that it ignores the bank's role, which is actually "[t]he critical distinction between commercial banking and investment banking." (251A.)

Judge Robb also rejected the majority's focus on factors such as low default rates and sophistication of investors, pointing out that by "[r]elying on these factors, a bank could transform 'transactions unquestionably at the heart of the securities industry into permissible activity for commercial depository banks.' " (252A.) Judge Robb observed that Congress flatly prohibited bank underwriting of corporate securities "without regard to the likely 'soundness' of the securities which a bank might sell." (255A.) As he stressed, the Act "has no provision permitting bank sales of securities which are 'prime quality' or 'very low-risk'." (253A.) Judge Robb also found that bank marketing of commercial paper gives rise to precisely the sort of potential abuses and hazards reviewed by this Court in *Investment Company Institute* v. *Camp*, 401 U.S. 617 (1971).

Finally, Judge Robb disagreed completely with the majority's attempt to "force a narrow meaning onto the terms of the Act." (256A.) In his view, the terms used by Congress—"stocks," "bonds," "debentures," "notes" and "other securities"—are all-encompassing and were intended to be so.

SUMMARY OF ARGUMENT

Point IA: Enacted following the economic chaos of the late 1920's and the ensuing banking crisis of the early 1930's, the Glass-Steagall Act was intended to separate commercial from investment banking as completely as possible. Section 16 of the Glass-Steagall Act flatly prohibits banks from underwriting "any issue of securities or stock," and section 21 of the Act equally precludes entities engaged in underwriting "stocks, bonds, debentures, notes, or other securities" from also accepting deposits. Remedial statutes in general should be construed broadly, and this Court has admonished specifically that the terms of the Glass-Steagall Act are to be applied literally and are *not* to be read narrowly. The majority below nevertheless refused to apply the statutory terms literally and gave them a "narrower" reading, to exclude the commercial paper at issue. The majority thereby contravened the admonitions of this Court, the language of the statute and the intent of Congress. Commercial paper by definition is a "note" and therefore is also a "security" under the plain meaning of the terms. Bank marketing of commercial paper thus is prohibited.

Point IB: Congressional intent to include commercial paper within the terms "notes" and "securities" as used in the Glass-Steagall Act is confirmed by its use of those terms in other legislation passed during 1933-35, along with the Glass-Steagall Act and its initial amendments. As this Court has confirmed, language used in contemporaneous statutes carries great weight in ascertaining Congressional intent. Congress broadly defined "securities" as including any "note" in several statutes enacted concurrently with the Glass-Steagall Act, but then expressly excluded commercial paper from coverage. Congress made no such exception for commercial paper in the Glass-Steagall Act, which broadly covers "notes" and "securities," and the legislative history of that Act contains no indication that such an exclusion was intended. The majority's attempt to write into the Glass-Steagall Act an exception for commercial paper that Congress itself omitted is thus unfounded and contrary to congressional history.

Point IIA: The majority below viewed the Glass-Steagall Act as allowing the Board to "adapt" the Act's underwriting prohibition on a "case-by-case basis" to accommodate the Board's view of "current business reality." Actually, Congress on several occasions rejected such a *regulatory* approach to the statute and chose instead flatly to *prohibit* banks from dealing in securities. For example, in 1932 Congress considered authorizing banks to continue underwriting securities under federal regulation and inspection but ultimately dropped that approach. Again, in 1935, when Congress considered the initial amendments to the Glass-Steagall Act, it specifically rejected an amendment that would have granted banks the authority "under regulation" to "underwrite and sell . . . notes." The Board, affirmed by the majority below, nevertheless by regulation has permitted banks to underwrite commercial paper based upon a host of factors (such as maturities, denominations and breadth of distribution) nowhere found in the statute. In effect, the Board unilaterally has assumed the sort of administrative authority that Congress repeatedly has denied.

Point IIB: The Board also applied a "functional analysis," under which it sought to determine whether commercial paper evidences a transaction "functionally similar to a commercial banking operation." Focusing that analysis solely on factors such as the sophistication of commercial paper issuers and investors, the Board ignored almost entirely the role of *banks* in the transactions, thereby again circumventing congressional intent. The Glass-Steagall Act was intended to protect the interests of *banks* and their depositors. Accordingly, if any "functional analysis" is to be undertaken under the Act, its focus throughout should be on the role of the *bank*. Historically, when banks had purchased commercial paper for their own account, the transactions served essentially as bank loans, with the banks assessing the commercial paper solely from the perspective of a lender. Here, the bank serves only as a middleman, selling third-party commercial paper to other investors. The commercial paper serves the same function as do securities for investment bankers—a vehicle for earning promotional or underwriting fees depending upon marketing successes. In marketing the paper, the bank is subject to the same

sort of "promotional incentives" and "pecuniary stake" that the Glass-Steagall Act was meant to prevent for depository institutions. Potential abuses and conflicts of interest between a bank's obligation to render disinterested financial advice and its incentives to earn fees, are inherent in its position—precisely the circumstance the Glass-Steagall Act was intended to prevent.

Point III: The decision below improperly defers to the Board's analysis of a purely legal issue of statutory construction, as to which the courts are the final authorities. Left standing, the majority decision will simply encourage other bank regulators to assume similar, unauthorized authority to make fundamental policy decisions that may only properly be made by Congress.

ARGUMENT

I.

THE GLASS-STEAGALL ACT PROHIBITS BANKS FROM UNDERWRITING COMMERCIAL PAPER

The Glass-Steagall Act was "a prophylactic measure directed against conditions that the experience of the 1920's showed to be great potentials for abuse." *Investment Company Institute* v. *Camp*, 401 U.S. 617, 639 (1971) ("*ICI* I"). Through the Act, Congress meant to "separat[e] as completely as possible commercial from investment banking. . . ." *Board of Governors* v. *Investment Company Institute*, 450 U.S. 46, 70 (1981) ("*ICI* II"). Sections 16 and 21 of the Act "flatly" and "entirely" prohibit banks from underwriting corporate securities. *Id.* at 58-59, n.24.

A. The Plain Language of the Act Prohibits Bank Underwriting of Commercial Paper

The question of statutory interpretation presented is whether short-term corporate notes, commonly referred to as commer-

cial paper,[4] are "notes" and/or "securities" within the meaning of sections 16 and 21 of the Act. Statutory construction, of course, starts with "the language of the statute itself."[5] The words used by Congress should be accorded "their ordinary, contemporary, common meaning,"[6] and, where unambiguous, that meaning "*must ordinarily be regarded as conclusive*."[7]

The terms of section 16 preclude banks from underwriting "any issue of securities or stock." Section 21, in turn, precludes entities engaged in underwriting "stocks, bonds, debentures, notes, or other securities" from simultaneously accepting deposits. This language itself demonstrates the expansive scope intended by Congress. As Judge Robb put it (256A-257A):

> The terms "stocks", "bonds", "debentures", and "notes" have broad meanings which encompass a multitude of different instruments. The term "other securities" further indicates the breadth of the Act's coverage; it catches any instruments which are not otherwise defined by the prior four terms. Taken as a group these five terms cover the spectrum of instruments a corporation might seek to market.

Commercial paper unquestionably constitutes "notes" as that word is commonly understood.[8] The Board and the

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4 As defined by the majority below, " '[c]ommercial paper' refers to prime quality, negotiable promissory notes bearing very short maturities—generally 30 to 90 days." (223A; footnote omitted.)

5 *E.g.*, *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 568 (1979).

6 *Perrin* v. *United States*, 444 U.S. 37, 42 (1979).

7 *American Tobacco Co.* v. *Patterson*, 456 U.S. 63, 68 (1982) (emphasis added; citations omitted). *Accord*, *Aaron* v. *SEC*, 446 U.S. 680 (1980); *Lewis* v. *United States*, 445 U.S. 55 (1980).

8 The term "note" is conventionally defined as "a written promise of the maker to pay a certain sum of money to the person named as payee, on demand or at a fixed or determinable future date." Munn, *Encyclopedia of Banking and Finance*, 698 (7th ed. 1973) ("Munn").

majority below both agreed that commercial paper comprises unsecured, short-term promissory *notes*. (122A, 223A.) It is equally clear that, as a note, commercial paper is a "security," under any common-sense definition of the term.[9] Congress' juxtaposition of the terms "notes" and "other securities" in section 21 of the Act confirms that it viewed notes as merely one type of "securities" for purposes of that section and thus, logically, for purposes of section 16 as well. *See ICI* I, 401 U.S. at 635. In sum, the language of these sections, on their face, plainly precludes banks from underwriting commercial paper. This should be "regarded as conclusive".

Indeed, if there were any ambiguity in these remedial provisions, which there is not, the presumption should be in favor of covering any instrument as to which there is a question. Remedial statutes are to be construed broadly, with their prohibitory terms enforced strictly. *E.g., Tcherepnin* v. *Knight*, 389 U.S. 332, 336 (1967). This Court has admonished, in *every* case which has considered the meaning of terms of the Glass-Steagall Act, that its prohibitions are not to be accorded a narrow or a technical meaning.[10]

The broad terms of sections 16 and 21, therefore, are to be applied "as they were written". *ICI* I, 401 U.S. at 639. This Court has "relied squarely on the literal language of §§ 16 and 21 of the Glass-Steagall Act . . . [and] recognized that the statutory language plainly applied." *ICI* II, 450 U.S. at 65. Specifically as to the term "securities," this Court has instructed:

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9 *E.g.*, Black's Law Dictionary, 1215 (5th ed. 1979) (defining "securities" as "[e]vidences of debts or of property" and specifically including "notes" as a form of securities); Munn, *supra*, at 828 (defining "securities" to include "notes . . . of every kind").

10 *See ICI* II, 450 U.S. at 65; *ICI* I, 401 U.S. at 635; *Board of Governors* v. *Agnew*, 329 U.S. 441, 446-47 (1947); *Awotin* v. *Atlas Exchange National Bank*, 295 U.S. 209, 212 (1935) (construing terms of the McFadden Act reenacted as part of the Glass-Steagall Act).

> [T]here is nothing in the phrasing of either § 16 or § 21 that suggests a narrow reading of the word securities. To the contrary, the breadth of the term is implicit in the fact that the antecedent statutory language encompasses not only equity securities but also securities representing debt.

ICI I, 401 U.S. at 635.

The majority below nevertheless decided that the terms "notes" and "securities" should *not* be construed literally, but rather should be accorded a "narrower meaning." (235A.) The "narrower meaning," however, was not that all commercial paper is excluded from the Act. Rather, deferring to the Board, the majority held that the basic terms "notes" and "securities" exclude only "prime quality commercial paper, of maturity less than nine months, sold in denominations of over $100,000 to financially sophisticated customers rather than to the general public." (249A-250A.) At the same time, the majority conceded that "another type of commercial paper—*e.g.*, of smaller denominations, or issued to the general public—might be a 'security' under the Glass-Steagall Act." (250A.)

That the Board and the majority found it necessary to resort to this sort of "now-you-see-it-now-you-don't" definition of "notes" and "securities" alone confirms the wisdom of this Court's repeated admonition that the terms are to be construed broadly and applied literally.

Nor does the majority's reasoning support its result. The majority found that the language of the Act can be read as barring banks only "from trading in specified instruments for raising capital as part of the permanent financial structure of a corporation" and "implicitly" permitting banks to underwrite all other debt instruments.[11] (235A-236A.) As noted, however, the majority specifically limited its holding to prime quality, large denomination notes sold only to sophisticated pur-

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11 Actually, if Congress had intended such a limited scope, it would have said so explicitly, as it has done in the banking laws in other contexts. *E.g.*, 12 U.S.C. § 321 ("capital notes").

chasers—factors that have nothing whatever to do with whether the notes are capital raising instruments. Conversely, the majority thought that smaller denomination or more broadly distributed commercial paper could well be "securities" under the Act, again without any reference at all to whether they are used for raising capital.

The majority also inappropriately parsed the Act, interpreting sections 16 and 21 separately from one another, even though this Court has recognized the congruity of these sections and has construed them together. *See ICI* I, 401 U.S. at 635. The two sections are reflections of one another, both intended to separate commercial and investment banking. For the majority to conclude (233A) that underwriting "notes," expressly prohibited by section 21, is not prohibited by section 16 because the latter refers to securities or stock, but "in no way refers explicitly to notes" (233A), is simply to miscast the statutory structure.

Considering section 16 in isolation, the majority went so far as to indicate that Congress supposedly did not intend to prohibit bank "underwriting" of all notes because it permitted banks to "discount and negotiate" promissory notes. (233A.) Not only were the terms, which have very different meanings,[12] added to the statute 70 years apart,[13] but if the majority were correct, banks have for more than a century had the authority to underwrite commercial paper. Yet, there is no evidence that banks generally did so previously and they certainly have not

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12 *Compare* Munn, *supra*, at 650-651 and U.C.C. § 3-202 *with* Munn, *supra* at 912 and Securities Act of 1933, § 2(11)g, 15 U.S.C. § 77b (11).

13 The authority for national banks to exercise "all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes," was included as part of the original National Bank Act of 1864, c. 106 § 8, 13 Stat. 101. The express prohibition against "underwriting" was not added until 1933 in the Glass-Steagall Act.

done so since the Glass-Steagall Act was passed.[14] As recognized in *BankAmerica Corporation* v. *United States*, ____ U.S. ____, 103 S.Ct. 2266, 2272-73 (1983), such consistent conduct over many years reflects "what was universally perceived as plain statutory language" and further indicates that the Act should be "interpreted according to its plain meaning."

The majority equally misconstrued the language of section 21, which prohibits banks from underwriting "stocks, bonds, debentures, notes, or other securities." To support its conclusion that section 21 had a restricted coverage, the majority read this language in reverse, concluding that section 21 covers only those "securities" that are in the nature of "notes" that, in turn, are in the nature of "debentures" and "bonds". (234A-235A.) If Congress had intended the statute to be read backwards, however, it would have written it that way. It did not.

As enacted, the language of section 21 shows that Congress intended the broadest possible coverage, with the term "other securities" encompassing any instruments not specifically listed. (256A-257A, Robb, J.) When Congress uses a series of broad exemplars, as it has here, such language "offers no indication whatever that Congress intended [a] limiting construction." *Harrison* v. *PPG Industries, Inc.*, 446 U.S. 578,

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14 The majority below cited the fact that banks had "dominated" the commercial paper market since the 19th century (238A, n.56), ignoring completely that until now the banks' role was as *purchaser* of commercial paper not as distributor. *E.g.*, Steiner, *The Commercial Paper Business*, 7 Fed. Res. Bull. 920, 923 (1921); Federal Reserve Bank of Chicago, *A Larger Role for Commercial Paper* 4, 9 (1968). Before the Glass-Steagall Act was passed, banks did *not* regularly distribute commercial paper, although some smaller banks are believed to have undertaken limited distribution as an accommodation to an existing customer. There is no evidence that banks acted as commercial paper underwriters at all after the Act was passed. Foulke, *The Commercial Paper Market* 107-108 (1931); Greef, *The Commercial Paper House* 379, 403-04 (1938); Selden, *Trends and Cycles in the Commercial Paper Market* 11-13 (1963).

588-89 (1980). This is a classic example of a court's creating ambiguity where there is none and, having done so, misconstruing the plain language used by Congress.[15]

Moreover, in concluding that commercial paper notes are not notes in the nature of "bonds" and "debentures"—which terms the majority construed as exclusively "long-term investment securiti[es]" (234A)—the majority overlooked that bonds and debentures are also issued in short maturities, some shorter than the maturities of the commercial paper at issue.[16] Conversely, while technically of short-term duration, commercial paper notes are often "rolled over" regularly to provide an on-going source of long-term funds for the issuer.[17]

The majority's further conclusion that Congress supposedly intended to remove banks only from "participation in 'speculative' securities markets" (236A) makes no sense against the

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15 *See id.* Maxims of statutory construction are not to be applied so as to "obscure and defeat the intent and purpose of Congress." *United States* v. *Alpers*, 338 U.S. 680 (1950). *See United States* v. *Turkette*, 452 U.S. 576 (1981); *United States* v. *Powell*, 423 U.S. 87, 91 (1975).

16 *E.g.*, *Wall Street Journal*, Oct. 27, 1983 at 40 (Port Authority of New York and New Jersey, notice of public offering including seven-month bonds); *id.*, Oct. 17, 1983 at 45 (Triborough Bridge and Tunnel Authority, notice of public offering including three-month revenue bonds); *id.*, Oct. 5, 1983 at 42 (South Dakota Student Loan Assistance Corporation, notice of public offering including nine-month revenue bonds).

17 The virtual impossibility of tracing a particular source of funds to working capital or fixed capital uses makes it impossible to establish whether the proceeds from commercial paper actually are being used for short-term, current transactions. Handal, *The Commercial Paper Market and the Securities Act*, 39 U. Chi. L. Rev. 362, 389 (1972); Federal Reserve Bank of Chicago, *A Larger Role for Commercial Paper*, 2, 12 (1968). Accordingly, commercial paper can be and is used to finance an issuer's long-term needs. *E.g.*, Securities and Exchange Commission, No-Action Letters, Liberty National Corp., May 6, 1983 (commercial paper proceeds used, in part, to finance mortgage loans and mobile home loans); First Jersey National Corp., June 4, 1981 (commercial paper proceeds used to acquire bank subsidiary).

overall statutory structure. Congress specified in great detail, both when the Act was passed and in subsequent amendments, a series of at least 15 separate U.S. government or general obligation municipal securities (*i.e.*, very low risk securities) in which *it* has decided that trading by banks is to be permitted. 12 U.S.C. § 24 (Seventh) (Supp. IV 1980). These statutory exceptions would have been unnecessary if Congress had already excluded "low risk" securities generally from the reach of the Act.[18] Instead, Congress specifically defined what securities are not too "risky" for purposes of the Act.[19] As Judge Robb noted, the Act simply "has no provision permitting bank sales of securities which are 'prime quality' or 'very low risk'." (253A.)

In plain language, the Glass-Steagall Act flatly and unambiguously prohibits banks from underwriting all corporate "notes" and "securities," including those notes referred to as commercial paper. For this reason alone the decision below should be reversed.

B. Contemporaneous Congressional Action Confirms that Commercial Paper Was Intended to be Covered by the Act

Confirmation, if confirmation were needed, that Congress intended commercial paper to be within the prohibition against bank underwriting of "notes" and "securities" can be found in Congress' contemporaneous use of the term "security" in several related statutes:

Securities Act of 1933, 15 U.S.C. §§ 77a, et seq.: Congress enacted this statute just three weeks before it passed the

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18 Also, if Congress intended only "speculative" securities to be covered by the Act, its express exception in section 16, permitting banks to purchase "investment securities" (*i.e.*, securities that are "not predominantly speculative," 12 C.F.R. § 1.3(b)), would be superfluous.

19 *Baker, Watts & Co.* v. *Saxon*, 261 F. Supp. 247 (D.D.C. 1966), *aff'd sub nom., Port of New York Authority* v. *Baker, Watts & Co.*, 392 F.2d 497 (D.C. Cir. 1968) (trading in securities, be they "gilt-edged" or otherwise, is proscribed).

Glass-Steagall Act. The two statutes were being considered by the same congressional committee at the same time. During the committee hearings on the Securities Act, Senator Glass attempted to persuade Congress to exclude "9 months commercial paper" from the definition of "security" in order to avoid interfering with ordinary bank lending transactions.[20] Congress rejected this exclusion, refusing to insert an exception for commercial paper and broadly defining "security" to include any "note." *See* 15 U.S.C. § 77b(1). To accommodate Senator Glass' concern, however, commercial paper was specifically exempted from the Act's registration and prospectus requirements.[21] Congress' consideration and rejection of the Glass amendment leaves no doubt that it understood commercial paper to be a "security" and a "note" as those terms are commonly understood.

Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, et seq.: During 1934 and 1935, when Congress was considering amendments to the Glass-Steagall Act proposed by the Comptroller of the Currency and others,[22] it was also considering the bill which became the Securities and Exchange Act. *See Hearings on H.R. 5357 Before the House Committee on Banking and Currency*, 74th Cong., 1st Sess. 179-80 (1935)

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20 *See Hearings on S. 875 Before the Senate Committee on Banking and Currency*, 73rd Cong., 1st Sess. 98 (1933).

21 Section 3(a)(3) of the Securities Act exempts from the Act's registration and prospectus requirements, but *not* from its definition or antifraud provisions:

> *[a]ny note*, draft, bill of exchange, or banker's acceptance which arises out of a current transaction or *the proceeds of which* have been or *are to be used for current transactions, and which has a maturity* at the time of issuance of *not exceeding nine months*. . . . (Emphasis added.)

15 U.S.C. § 77c(a)(3).

22 *See, e.g.*, Annual Report of the Comptroller of the Currency, 8-12 (Jan. 3, 1934); *Hearings on S.1715 and H.R. 7617 Before the Senate Committee on Banking and Currency*, 74th Cong., 1st Sess. 113 (1935); *Hearings on H.R. 5357 Before the House Committee on Banking and Currency*, 74th Cong. 1st Sess. 661 (1935).

(testimony of Federal Reserve Board Chairman, Marriner S. Eccles, recognizing the contemporaneous enactment and similarity of purpose of these statutes). In enacting the Securities Exchange Act in 1934, however, Congress expressly excluded commercial paper from the Act's definition of "security"—which otherwise included any "note" (15 U.S.C. § 78c(a)(10))—again confirming its understanding that commercial paper would be considered a "security" under the ordinary meaning of that term, unless an express exception were provided.

Public Utility Holding Company Act of 1935, 15 U.S.C. §§ 79 et seq.: Congress considered this Act at the same time it was debating the proposed amendments to the Glass-Steagall Act that were ultimately encompassed in the National Banking Act of 1935, c.614, §§ 303, 308, 49 Stat. 707. These statutes were enacted on successive business days—Friday, August 23 and Monday, August 26, 1935, respectively. In the National Banking Act of 1935 Congress, *inter alia*, changed the term "investment securities" in section 16 to "securities and stock." 12 U.S.C. § 24 (Seventh). In the Public Utility Holding Company Act, Congress prohibited registered holding companies from acquiring any "securities" but permitted purchase of "*such commercial paper and other securities*" as the Securities and Exchange Commission might allow by rules and regulations. 15 U.S.C. §§ 79b(a)(16), 79i(c)(3). Again, as shown by its use of the phrase "and *other* securities," Congress unquestioningly understood commercial paper to be a type of "security" within the plain meaning of that term. *See also*, H.R. Rep. No. 1318, 74th Cong., 1st Sess. 15 (1935) ("a third class of securities permitted under this subsection is commercial paper").

Express Congressional language used in contemporaneous statutes, as this Court has instructed, reveals " 'the meaning of the words as used in their contemporary setting,' " and is " 'entitled to great weight in resolving any ambiguities and doubts.' " *Erlenbaugh* v. *United States*, 409 U.S. 239, 244 (1972), *quoting United States* v. *Stewart*, 311 U.S. 60, 64-65

(1940). Against history recited above, it is patently illogical to conclude, as did the Board (132A) and the majority below (236A-238A), that Congress did not understand commercial paper to be a "security" when it enacted the Glass-Steagall Act.

The absence of specific discussion concerning commercial paper underwriting during congressional debates on the Glass-Steagall Act, cited by the majority (236A), is hardly surprising. No discussion should be expected, in that with rare exceptions banks then were not dealing in commercial paper. (*See supra*, n.14.) Their activities had been limited to purchasing commercial paper for their own accounts (*i.e.*, lending), and that was the purport of the little congressional discussion which occurred.[23] In any event, the *lack* of congressional discussion on a topic cannot be turned into the "rare and exceptional circumstances" needed "to make plain the intent of Congress that the letter of the statute is not to prevail."[24]

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23 Senator Walcott, floor manager of the Glass bill, for example, was concerned that corporations had stopped meeting their financial needs "by borrowing at commercial banks upon their commercial paper—that is, upon their notes." 75 Cong. Rec. 9904 (1932) (emphasis supplied). Not only were "commercial paper" and "notes" thus viewed as synonymous, but the correct role for banks was regarded to be that of lenders, i.e., purchasers, of commercial paper for their own accounts.

24 *Crooks* v. *Harrelson*, 282 U.S. 55, 60 (1930), *quoted in Rubin* v. *United States*, 449 U.S. 424, 430 (1981) and *TVA* v. *Hill*, 437 U.S. 153, 187 n.33 (1978).

The majority also cited Representative McFadden's earlier statement that commercial paper was not considered an investment security under the McFadden Act of 1927. The majority reasoned that banks therefore were "left free to trade in commercial paper without restriction" after that statute was enacted. (237A-238A.) But, the majority had it backwards. Banks never had the authority "to trade in commercial paper," and the significance of the McFadden statement is simply that no such authority was provided even under the McFadden Act, which marked the first time Congress expressly recognized the authority of banks to deal in investment securities. *See Awotin v. Atlas Exchange National Bank*, 295 U.S. 209, 212 (1935). Because of their

It is equally unsound to reason that Congress intended in the Glass-Steagall Act *implicitly* to make the distinction between commercial paper notes and notes generally, that it made *explicitly* in the other statutes discussed above. As this Court instructed in another context:

> Had Congress intended so fundamental a distinction, it would have expressed that intent clearly in the statutory language or the legislative history. It did not do so, however, and it is not this court's function "to sit as a super-legislature," *Griswold* v. *Connecticut*, 381 U.S. 479, 482 (1965), and create statutory distinctions when none were intended.[25]

The Board, in essence, sought to take the express exception for commercial paper included in other contemporaneous statutes and administratively engraft it onto the Glass-Steagall Act. (136A, n.26.) But, as this Court held in construing a different statute in *Erlenbaugh* v. *United States*, *supra*, to do so would "carve a substantial slice from the intended coverage of the statute. This we will not do without an affirmative indication—which is lacking here—that Congress so intended." *Id.*, 409 U.S. at 247.

In sum, congressional action contemporaneous with the consideration, enactment and initial amendment of the Glass-Steagall Act confirms what is apparent from its plain language: commercial paper is both a "note" and a "security" within its coverage, and bank underwriting of it is prohibited. For this reason also, the decision below should be reversed.

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express authority to discount and negotiate promissory notes, however, banks could continue to purchase commercial paper for their accounts as they had been doing for years. And, contrary to the majority's further view (238A, n.59), banks can thereby continue to do so now.

25 *American Tobacco Co.* v. *Patterson*, *supra*, 456 U.S. at 71, n.6. *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 572 (1979) (when Congress wished to provide an exception to a statute "it knew how to do so and did so expressly").

II.

THE REGULATORY APPROACH ADOPTED FRUSTRATES THE CONGRESSIONAL POLICY UNDERLYING THE GLASS-STEAGALL ACT

The decision of the majority below has an even broader significance than its distortion of the plain language of the Act. It effectively transforms the Act's absolute prohibitions into mere regulatory guidelines subject to *ad hoc* administrative adjustment—directly contrary to congressional intent.

A. The Majority Below Sanction the Exercise of Discretionary Authority Expressly Withheld by Congress

The majority viewed the Glass-Steagall Act as permitting the Board to "adapt" the flat prohibition against bank underwriting on a "case-by-case basis" to accommodate the Board's view of "current business reality." (228A.) But the Glass-Steagall Act was an unusual statute. Unlike other contemporaneous legislation conferring discretionary, regulatory authority,[26] the Act was a prohibitory statute, the terms of which are to be construed broadly and applied literally. *ICI* I, 401 U.S. at 639. Nothing in the statute itself or its legislative history supports the majority's regulatory approach.

Congress considered proposals merely to regulate, rather than prohibit, securities underwriting by banks when it initially formulated the Act, when it enacted the initial amendments to the Act, and repeatedly thereafter. Each time, Congress rejected the regulatory approach.

Early proposals considered by the Senate Banking Committee in 1932, for example, would have authorized banks to continue dealing in and underwriting securities of private issuers under federal regulation and inspection. The proposals

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26 *See infra*, p. 24 & n.31.

were dropped.[27] Congress was obviously convinced that a more "drastic step"[28] was necessary. As Senator Bulkley, a senior member of the Senate Banking Committee, put it at the time the Glass-Steagall Act was being considered:

> If we want banking service to be strictly banking service, without the expectation of additional profits in selling something to customers, we must keep banks out of the investment security business.

75 Cong. Rec. 9912 (1932); cited approvingly in *ICI* I, 401 U.S. at 635. To achieve this, Congress enacted the flat prohibitions found in sections 16 and 21 of the Act.

In marked contrast with section 32 of the Act, 12 U.S.C. § 78, which permits the Board to exempt certain arrangements from the Act's management interlock provisions,[29] neither section 16 nor section 21 vests *any* exemptive authority whatsoever in the Board. The *only* administrative authority contained in the latter sections authorizes the Comptroller of the Currency "by regulation" to permit banks to purchase invest-

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27 *See* Willis and Chapman, *The Banking Situation* (1934). The Senate Banking Committee drafted legislation that would have allowed continued underwriting activities by banks subject to federal inspection and regulation, under penalty of expulsion from the Federal Reserve System. This proposal was ultimately dropped in favor of the complete separation of commercial and investment banking in response to "great numbers of letters from citizens of all classes . . . who demanded absolute elimination of [bank securities affiliates]—root and branch—from the national banking and Federal Reserve systems." *Id.* 68-69.

28 *ICI* I, 401 U.S. at 629.

29 Section 32 of the Act prevents officer, director or employee interlocks between member banks of the Federal Reserve System and any entity engaged in securities distribution or sale. It provides, however, that "in a limited class of cases" the Board may allow interlocks "when in the judgment of the Board it would not unduly influence the investment policies of such member bank or the advice it gives its customers." 12 U.S.C. § 78.

ment securities for their own account, not to deal in or underwrite them.

In 1935 Congress actually considered providing similar regulatory authority to permit bank underwriting of securities. The version of the Banking Act of 1935 passed by the Senate included a provision amending section 16 of the Glass-Steagall Act to permit "national banks, under regulation by the Comptroller of the Currency, to *underwrite and sell* bonds, debentures, and *notes*."[30] This of course is precisely what the Board has authorized here. But the House refused to provide this regulatory authority, and the Conference Committee struck the Senate provision. Conf. Rep. No. 1822, 74th Cong., 1st Sess. 53 (1935). The amendments of 1935, as enacted by Congress, continued the flat prohibitions in sections 16 and 21 against bank underwriting of securities.

This Congressional action is all the more important in light of the differing approach it followed during 1933-35 in enacting the federal securities laws. In those statutes Congress chose to *regulate*, rather than prohibit, a number of activities, leaving the limits of statutory coverage to subsequent discretionary administrative action.[31] By contrast, in the Glass-Steagall Act Congress spoke as broadly as possible to *prohibit*, in advance, certain activities.

The absolute approach chosen by Congress in the Glass-Steagall Act is also underscored by contrast with more recent

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30 S. Rep. 74-1007, 74th Cong., 1st Sess. 16 (1935) (emphasis supplied). At the urging of the Comptroller of the Currency and others, Congress, during 1934-1935, considered various amendments proposed to the Act as it had been passed 100 days after President Roosevelt originally declared the five-day national banking holiday in 1933. *See supra*, p. 18, n.22.

31 *E.g.*, Securities Act of 1933, § 2, 15 U.S.C. § 77b; Securities Exchange Act of 1934, §§ 3, 15(a)(2), 23(a), 15 U.S.C. §§ 78c, 78o(a)(2), 78w(a). *See also*, Public Utility Holding Company Act of 1935, §§ 9, 20, 15 U.S.C. §§ 79i(c)(3), 79t.

banking legislation such as the Bank Holding Company Act, 12 U.S.C. § 1841, *et seq.* There, Congress did vest discretionary power in the Board to authorize bank holding companies to engage in those activities the Board finds to be "so closely related to banking as to be a proper incident thereto." 12 U.S.C. § 1843(c)(8). But, as congressional debate over amendments to the Bank Holding Company Act during 1970 again confirmed, the Glass-Steagall prohibitions were not to be diluted. Senator Sparkman, floor manager of the 1970 amendments, explained in responding to concern about their effect upon the Glass-Steagall Act:

> As it now stands, the Glass-Steagall Act broadly prohibits both banks and their affiliates from engaging in what we commonly understand to be the securities business. . . . [W]e did not intend to amend or modify, directly or indirectly, any limitations on the activities of banks, bank holding companies or any of their affiliates, now contained in the Glass-Steagall Act. If Congress is to change that longstanding, fundamental statement of public policy, we will have to do so in other legislation.

116 Cong. Rec. 42430 (1970), quoted in *ICI* II, 450 U.S. at 75, n.55. No such "other legislation" has been enacted, and the Glass-Steagall prohibitions remain to be enforced strictly pursuant to Congress' "longstanding, fundamental statement of public policy."

Defying these repeated expressions of congressional intent, however, the majority has now construed the Act as permitting banks to underwrite notes, depending upon the Board's administrative view of a number of specific factors having no basis in the statutory language:

- — the denominations of the instrument being sold;
- — the breadth of distribution of the instruments;
- — the degree of sophistication of the purchasers of the instruments;

— the financial strength of the entity issuing the instruments;

— the use to which the proceeds will be put by the issuing entity; and

— the amount of instruments previously underwritten for that issuer by the distributing banks.[32]

The Board, affirmed by the majority below, has simply—and incorrectly—assumed the sort of regulatory authority denied by Congress throughout half a century. The uncertainty of *ad hoc* administrative enforcement has replaced the certainty of Congress' prospective prohibition. The Act's flat statutory bar against underwriting of "notes or other securities" has become a regulatory filigree through which just such underwriting may pass.[33]

It is especially significant that this action comes at a time when Congress itself has been considering major legislative proposals to alter existing federal restrictions on financial institutions. In each of several recent sessions Congress has

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32 *See* Federal Reserve System, *Policy Statement Concerning the Sale of Third Party Commercial Paper by State Member Banks*, 46 Fed. Reg. 29333 (June 1, 1981) (the "guidelines"). (183A.)

33 The impact of the Board's ruling has not been limited to the securities and banking industries: it has already affected the carefully balanced regulatory system governing the nation's financial system. For example, because of what it described as the "abrupt change" effected by the Board's action allowing banks "for the first time" to underwrite securities, the Federal Energy Regulatory Commission was required immediately to issue a temporary blanket exemption from certain provisions of the Federal Power Act, 16 U.S.C. § 825d(b). *See* Order in Docket No. EL 81-5-000, March 27, 1981, 46 Fed. Reg. 19980 (April 2, 1981); 171A. The Securities and Exchange Commission was required to respond similarly to the Board's ruling, pursuant to its responsibilities under the Public Utility Holding Company Act. *See* SEC, Public Utility Holding Company Act Release No. 35-21967 (March 18, 1981), 46 Fed. Reg. 18535 (March 25, 1981).

enacted major reforms to the federal banking laws.[34] Not only has Congress expressly reaffirmed its opposition to administrative readjustment of the Glass-Steagall prohibitions,[35] but, in each instance, Congress has failed to modify the Glass-Steagall underwriting restrictions in the slightest.

In sum, fifty years of congressional history confirms that the prohibitions of the Glass-Steagall Act are to be applied broadly, as they were written. Any restriction of the Act's scope "must be implemented by Congress and not by a crabbed [administrative] interpretation of the words of the statute." *BankAmerica Corporation* v. *United States*, *supra*, 103 S.Ct. at 2273.

B. The "Functional Analysis" Adopted by the Majority Below Contravenes the Fundamental Objective of Congress

Even if a regulatory approach in general had been appropriate under the Act, the specific "functional analysis" employed by the Board and embraced by the majority below was not. Applied consistently with congressional intent, a "functional analysis" yields a result opposite to that reached below.

The stated objective of the functional analysis proposed by the Board was to determine whether commercial paper evidences a transaction "functionally similar to a traditional

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34 *See* Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 132 (1982); Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132 (1980); Financial Institutions Regulatory and Interest Rate Control Act of 1978, Pub. L. No. 95-630, 92 Stat. 3641 (1978).

35 In the Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, 94 Stat. 132 (1980), Congress extended to the Comptroller of the Currency authority for the first time to issue such rules as are needed to "carry out the responsibilities of the office," but specifically reaffirmed in the statute that the Comptroller had *no* general authority to issue regulations concerning "securities activities of National Banks under the Act commonly known as the 'Glass-Steagall Act'." 12 U.S.C. § 93a.

commercial banking operation." (242A.) If so, under the Board's reasoning, the instruments involved are outside the Act's coverage. Again adhering to the Board's logic, the majority below examined the characteristics of commercial paper, of its issuers and of its purchasers, but ignored the role of the *bank*. In so doing, both the Board and the majority missed the basic point of the statute.

The Glass-Steagall Act was intended to separate investment from commercial banking as completely as possible. *ICI* II, 450 U.S. at 70. As Judge Robb recognized in dissent, because "[t]he critical distinction between commercial banking and investment banking is the bank's role in the transaction," any interpretation of the Act "must focus on the bank's role in the transaction with a view to maintaining the Act's separation of functions." (251A-252A.) *See also*, Note, *A Conduct-Oriented Approach to the Glass-Steagall Act*, 91 Yale L. J. 102 (1981).

A functional analysis viewed from the perspective of the bank leaves little question that the bank's handling of the commercial paper in question falls squarely within the Act. The majority below brushed off the difference between the traditional role of a bank in purchasing commercial paper, and this bank's proposed role of marketing the paper, as the bank's simply being "on the other side of the transaction." (246A.) As Judge Robb put it, however, "this distinction . . . is determinative under the Act." (251A.)

There is a vast difference between a bank *purchasing* commercial paper and a bank *distributing* commercial paper. Historically, when banks purchased commercial paper,[36] the transactions were essentially the same as if the corporate issuer had come into the bank and obtained a bank loan in the amount of the discounted value of the commercial paper. Either way, the bank was lending money to the corporation and deriving its revenue from the interest (or discount) accruing to it. As a lender, the sole concern of the bank was to assess the loan as a risk.

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36 *See supra*, n.14.

In stark contrast, the bank here is not in any sense lending money to issuers of commercial paper. The bank's function is solely that of a marketer, which will earn its fees based upon its success in distributing the commercial paper of the issuers.[37] The commercial paper thus serves the same function for the bank that securities serve for investment bankers. The concern of a bank so involved is no longer simply to assess the paper as a lending risk, but rather to assess the paper as a vehicle for earning sales commissions or fees.

Reference to the factors relied upon by the majority, such as the sophistication of investors, the stability of issuers and the quality of investments, "provides no help in determining whether the bank's role in the transaction violates the Act." (Robb, J. 252A.) Reliance on such factors would permit banks to "transform 'transactions unquestionably at the heart of the securities industry into permissible activity for commercial depository banks.' " (*Id.*) Sophisticated investors and financially sound issuers frequently deal in high quality stocks and low-risk securities, but there is no doubt that such instruments are within the prohibitions of the Act.

The factors considered by the majority may be important in determining the application to particular instruments of other statutes, such as federal securities laws, because those statutes are intended to protect the interests of *investors*.[38] Yet, such factors have no bearing upon whether *banks* should be dealing in the instruments, which is the concern of the Glass-Steagall Act.[39] Summarizing the purpose behind sections 16 and 21 in *ICI* I this Court stated:

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37 *See* Judge Robb's dissent, contrasting a bank's role as "lender," when it purchases commercial paper, and a bank's role as "seller," when it markets the paper. (251A.)

38 *See, e.g., Tcherepnin* v. *Knight*, 389 U.S. 332, 336 (1967); *SEC* v. *Howey Co.*, 328 U.S. 293, 298-299 (1946).

39 As the majority below said, in seeking to dismiss the relevance to this case of definitions contained in the securities laws: "A different focus of analysis is called for under the Glass-Steagall Act, which aims

> Congress acted to keep commercial banks out of the investment banking business largely because it believed that the promotional incentives of investment banking and the investment bankers pecuniary stake in the success of particular investment opportunities was destructive of prudent and disinterested commercial banking and of public confidence in the commercial banking system.

ICI I, 401 U.S. at 634.

In *ICI* I this Court rejected administrative contentions, analogous to those of the Board here, that the activity at issue was permissible because of its relation to traditional bank activities.[40] Because the plan was "of a different character" from the historic bank role, and "in direct competition with" the mutual fund industry, it was held to be contrary to the prohibitions of the Glass-Steagall Act. *ICI* I, 401 U.S. at 625, 628. Here, too, the bank's activity will inevitably "give rise to a promotional or salesman's stake in a particular investment" and "will involve an enterprise in direct competition with aggressively promoted" commercial paper sold by investment bankers. *ICI* I, 401 U.S. at 638.

The promotional materials in the record reflect just such competition. They describe the bank's fee as "competitive with that of commercial paper dealers" (61A); refer to a sales distribution network that can "expand your commercial paper sales in a way that our competitors (either bank or dealer) cannot" (63A); and state that "unlike the investment bankers" the bank is "necessarily a short-term money market expert" (69A). In fact, potential customers are told that, even if the bank fails to sell all of an issuer's commercial paper, the bank

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at protecting the integrity of *banks* and the financial resources of *depositors* rather than *investors*." (241A; emphasis in original.)

40 The Comptroller contended that the bank's plan for collective investment of managing agency accounts was simply a derivative of the bank's powers to commingle trust funds and to act as a managing agent, both of which concededly were proper under the banking laws.

in effect will buy the balance for its own account, at its own risk, with a view toward possible resale.[41]

It is no accident that the bank makes these representations. They concern the type of services offered generally by commercial paper dealers. If the bank is to be "completely competitive" as it says (65A), so, too, must it offer the services. This Court's warning in *ICI* I applies equally here:

> When a bank puts itself in competition with mutual funds, the bank must make an accommodation to the kind of ground rules that Congress firmly concluded could not be prudently mixed with the business of commercial banking.

ICI I, 401 U.S. at 637.

Significantly, the Board acknowledged in its ruling that: "[T]he sale of third party commercial paper by a commercial bank could involve, at least in some circumstances, practices that are not consistent with principles of safe banking." (141A.) The Board then issued guidelines relating to the sale of commercial paper notes by banks (183A), but such action is not, and cannot be, a sufficient response. The Glass-Steagall Act was meant to eliminate, not merely to "minimize," the potential for abuse that is *inherent* in the combination of investment and commercial banking. As this Court stated repeatedly in *ICI* I, Congress enacted the Glass-Steagall Act not just to remedy existing abuses but to avoid "*potential*" hazards that "*might*" arise.[42] 401 U.S. at 637-38 (emphasis supplied); *see also*, *ICI* II, 450 U.S. at 66-67, n.38.

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41 The promotional materials in the record show that where the bank is unable to place all of an issuer's commercial paper, it may loan the issuer short term funds, "using the unsold paper as collateral". (37A.)

42 Indeed, any number of conflicts of interest are inherent in a bank's marketing of commercial paper. For example, if a bank sells commercial paper issued by one of its customers who subsequently has a need for money to "retire" the paper at maturity, the bank may feel compelled to lend the customer the money to do so. Additional conflicts and pressures are inherent in any transaction in which a bank

Nor do the factors that the Board seeks to regulate eliminate the hazards that bank underwriting of commercial paper presents. Penn Central's default on $82.5 million of commercial paper that, only three weeks earlier, had been marketed as "prime" quality and sold in large denominations to sophisticated purchasers,[43] dramatically confirms that no number of administrative "guidelines" can effectuate the Congressional purpose. As Judge Robb discussed at some length (253A-255A), the Board's present guidelines would have permitted banks to underwrite the Penn Central commercial paper, and yet such activities would have presented exactly the sort of hazards this Court cautioned against in *ICI* I, 401 U.S. at 630-33. The intent of Congress can only be carried out by prohibiting the activity entirely, which is precisely what the Glass-Steagall Act was designed to do.

In sum, the majority's "functional analysis" reflects the regulatory approach that Congress rejected and permits the potential risks that Congress prohibited. In so doing,

> [t]he majority's holding contravenes the fundamental policy of the Glass-Steagall Act . . . [which is] to insulate commercial banking from the hazards inherent in investment banking by mandating a complete separation of those two functions.

(250A; Robb, J. dissenting.) For this reason, too, the decision below should be reversed.

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agrees to market commercial paper issued by a corporation to pay down its outstanding loan from the bank. Again, if a bank sells commercial paper to a customer that subsequently has a need for cash before the commercial paper is due, the bank may feel obliged either to repurchase the paper or to extend a loan to that customer. These conflicts of course are multiplied where a bank takes commercial paper issued by one of its customers and sells it to yet another of its customers. In each instance the bank's role as an impartial source of credit is compromised by its role as a marketer.

43 Handal, *The Commercial Paper Market and the Securities Act*, 39 U. Chi. L. Rev. 362, 376-77 (1972). *See also* Securities and Exchange Commission, *The Financial Collapse of the Penn Central Company* (Aug. 1972).

III.

THE MAJORITY BELOW IMPROPERLY DEFERRED TO AN INCORRECT ADMINISTRATIVE DETERMINATION OF A PURELY LEGAL ISSUE

Reversing the District Court because it had supposedly given "insufficient weight" to the Board's expertise (226A), the majority below reached its conclusions "taking account of appropriate deference to the Board's expertise and administrative responsibility." (230A.) The majority defined its task as simply reviewing whether the Board's interpretation was "sufficiently reasonable" (227A). In so doing, the majority opinion raises fundamental questions concerning the judiciary's responsibility "to construe the language employed by Congress,"[44] and to enforce the separation of commercial banking from investment banking that Congress intended.

The majority opinion simply ignored this Court's direction in *Federal Election Comm'n* v. *Democratic Senatorial Campaign Comm.*, 454 U.S. 27, 31 (1981), that discussion of judicial deference to an administrative agency is "pointless" where, as here, an agency action "violate[s] the plain language of the Act as well as the statutory purposes revealed by legislative history."

The majority reasoned that the Board should be free to apply "general, undefined statutory terms" to "new facts". (228A.) Rather than being "undefined," however, the terms here are broad and self-defining. Also, the only "new facts" discussed have nothing to do with the instruments described by the terms ("notes" and "securities"), but exclusively concern the banks' new *use* of the instruments described. Commercial paper itself has been around for decades, and was well known

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44 *Zuber* v. *Allen*, 396 U.S. 168, 193 (1969); *Federal Maritime Comm'n* v. *Seatrain Lines, Inc.*, 411 U.S. 726, 745-46 (1973); *Espinoza* v. *Farah Mfg. Co.*, 414 U.S. 86, 93-95 (1973).

to Congress when it drafted the Act broadly to include "notes or other securities".[45]

The majority further stated that the Board "exercises broad rulemaking and adjudicative powers" and has "expert knowledge of commercial banking." (227A.) But, as discussed (*supra*, pp. 22-24), the Board has *no* rulemaking authority under the Glass-Steagall Act to permit securities underwriting by banks. And the Board "defined" the unambiguous statutory terms, not on the basis of matters within its expertise, but by resort to legislative history and the canons of statutory construction—matters within the unique expertise of the *judiciary*.[46] As the District Court below stated, the Board's decision resolved a purely legal issue resting "on inquiries familiar to all courts." (205A.) Under our system,

> the courts are the final authorities on issues of statutory construction. They *must* reject administrative constructions of the statute, whether reached by adjudication or by rule-making, that are inconsistent with the statutory mandate or that frustrate the policy that Congress sought to implement.[47]

The opinion below, if allowed to stand, will almost certainly signal to lower courts and federal regulators an abdication of the judiciary's role to prevent the administrative dismantling of this fundamental statute. In the face of congressional refusal to modify the Glass-Steagall Act restrictions,[48] federal banking

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45 *See supra*, pp. 17-20.

46 *Barlow* v. *Collins*, 397 U.S. 159, 166 (1970).

47 *Federal Election Comm'n* v. *Democratic Senatorial Campaign Comm.*, *supra*, 454 U.S. at 31 (emphasis supplied). *See also*, *American Ship Bldg. Co.* v. *NLRB*, 380 U.S. 300, 318 (1965) (resort to deference "cannot be allowed to slip into a judicial inertia in the unauthorized assumption by an agency of major policy decisions properly made by Congress").

48 *See supra*, pp. 26-27.

regulators have been under intense pressure from the institutions they regulate to relax unilaterally the previously recognized limits on bank activities.[49] Absent action by this Court, bank regulators are likely to continue assuming policy decisions of enormous economic significance that should properly be addressed only by Congress. It is therefore particularly important to reaffirm that "there are limits. . . on how far an agency may go in its interpretive role," and that deference cannot substitute for the judicial "obligation to honor the clear meaning of a statute, as revealed by its language, history and purpose." *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551, 566 & n.20 (1979).

CONCLUSION

The majority opinion should be reversed and the Board's ruling, as well as its guidelines implementing that ruling,[50]

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49 For example, the Comptroller of the Currency has repudiated his long-standing construction of the Glass-Steagall Act and ruled that national banks may establish subsidiaries to offer securities brokerage. *Decision of the Comptroller on the Application of Security Pacific National Bank* (Aug. 26, 1982). The Federal Deposit Insurance Corporation has proposed new rules to permit brokerage and underwriting activities by affiliates of the 9,000 state chartered banks under its jurisdiction. 47 Fed. Reg. 38984 (Sept. 3, 1982). And, The Federal Home Loan Bank Board has authorized the first nationwide joint venture by federally chartered savings and loan associations in approving a thrift-sponsored brokerage and investment advisory firm. *Decision of the FHLBB on the Service Corporation Application of Coast Federal Savings & Loan Association, et al.* (May 6, 1982). These decisions are now being challenged in the federal courts. *See, Securities Industry Ass'n* v. *Conover*, No. 82-2865, Slip Op. (D.D.C. Nov. 2, 1983); *Investment Company Institute* v. *United States*, No. 82-2532 (D.D.C. filed Sept. 8, 1982); *Securities Industry Ass'n* v. *Federal Home Loan Bank Board*, No. 82-1920 (D.D.C. filed July 12, 1982).

50 As the majority below put it: "[B]ecause the guidelines in essence describe Bankers Trust's activities, it would be difficult to reconcile those guidelines with the district court's holdings." (226A, n.17.)

should be declared null and void and the Board directed to act accordingly.

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